

Service Date: March 13, 1984

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

IN THE MATTER of The Application of The ) DOCKET No. 83.3.16  
Butte Water Company to Increase Water )  
Rates and Modify Rules and Regulations ) ORDER NO. 4978a  
for its Anaconda, Montana, Customers. )

\* \* \* \* \*

APPEARANCES

FOR THE APPLICANT:

Dennis R. Lopach, Attorney at Law, Hjort, Lopach and Tippy, P.O.  
Box 514, Helena, Montana 59624.

FOR THE INTERVENOR:

John Allen, Staff Attorney, Montana Consumer Counsel, 34 West  
Sixth Avenue, Helena, Montana 59620.

FOR THE COMMISSION:

Opal Winebrenner, Staff Attorney, 2701 Prospect Avenue, Helena,  
Montana 59620.

BEFORE:

Thomas J. Schneider, Chairman  
John Driscoll, Commissioner  
Howard L. Ellis, Commissioner

BACKGROUND

1. On March 14, 1983, Butte Water Company (Applicant or BWC)  
filed an application with the Montana Public Service Commission  
(Commission) for authority to increase rates and charges for  
water service  
to its customers in Anaconda, Montana. Applicant requested an

average

increase of approximately 8.28 percent, which constitutes a revenue

increase of approximately \$23,983 in annual revenues.

2. Concurrent with its filing for a permanent increase in rates, BWC filed an application for an interim increase in rates of 8.28 percent, equaling a revenue increase of approximately \$23,983 or 100 percent of the proposed permanent increase.

3. On May 3, 1983, the Commission, having considered the data filed with the Applicant's interim application, issued Order No. 4978 granting the Applicant interim rate relief in the amount of \$19,718 annually.

4. On October 19, 1983, pursuant to provisions contained in Commission Rule 38.2.1207, ARM, the Applicant filed revised exhibits and supplemental testimony which reflected certain very substantial changes in the filed revenues and expenses that occurred in 1983, and which could not be fully quantified at the time of the original filing. The impact of these revisions was to decrease the revenue increase request for its Anaconda service area from \$23,983 to \$19,168.

5. At the public hearing, the Applicant indicated its parent company, Anaconda Minerals, had recalculated pension expense attributable to the Anaconda, Montana, operations. The Applicant stated this recalculation resulted in an annual expense increase of \$1,453, and that this expense increase had not been included

in its revised exhibits submitted on October 19, 1983.

BWC requested that the Commission, during its deliberations on the merits of the Applicant's proposed rate adjustment, consider this additional expense increase as a possible offset against previously identified expense adjustments that may be disallowed by the Commission. The Applicant did not request an adjustment in the overall revenue increase request as previously filed on October 19, 1983.

Absent objections from any party participating in this proceeding, and being cognizant of the fact that the increased pension expense did not impact the overall revenue increase requested in this docket, the Commission agreed to consider the increased pension expense as a possible offset for any previously identified expense increases that may be disallowed.

6. At the public hearing, all parties agreed to a waiver of the 9-month deadline provided for in Section 69-3-302(1), MCA, and established a 60-day extension on this deadline as being a reasonable period within which the Commission should render its final decision.

7. At the public hearing, the Applicant presented the following witnesses:

Gary Mannix, President and General Manager of BWC  
Elmer Moke, Rate Consultant  
C.M. "Skip" Dunfee, Controller BWC

8. The Montana Consumer Counsel presented the testimony of three public witnesses at the hearing.

9. The year-ending December 31, 1982, test year was uncontested and is found by the Commission to be a reasonable period within which to measure the Applicant's utility revenues, expenses, and returns for the purpose of determining a fair and reasonable level of rates for water service.

#### ANALYSIS AND FINDINGS OF FACT

##### CAPITAL STRUCTURE

10. The Applicant proposed the following capital structure for rate case presentation:

<u>Description</u>	<u>Amount</u>	<u>Ratio</u>
Debt	\$3,888,889	124.2%
Equity	<u>(757,768)</u>	<u>(24.2%)</u>
TOTAL	\$3,131,121	100.0%

The capital structure proposed by the Applicant was not challenged by any party participating in this proceeding, and, therefore, is accepted by the Commission.

##### COST OF DEBT

11. The debt capital of the Applicant consists of a loan from the Atlantic Richfield Company (ARCO), its parent company, having a term of 10 years and carrying an interest rate of 14.04 percent. This loan arrangement was executed between the parties (BWC & ARCO) in compliance with this Commission's Order No. 4801a, wherein the Commission found that the loan arrangements then in existence were imprudent. The Commission finds the cost of this debt to be reasonable and is accepted by the Commission.

12. The Commission, based upon the testimony in this docket, finds that the Applicant should be allowed a debt cost of 14.04

percent, which is the interest rate applicable to the loan agreement entered into between BWC and ARCO.

The Commission will reiterate its statement from Order No. 4897a that it is the Commission's opinion that good business practice dictates that BWC examine the possibility of obtaining lower cost debt capital.

CAPITAL STRUCTURE AND COMPOSITE COST OF TOTAL CAPITAL

Weighted Description Cost	Amount	Ratio	Cost
Debt 17.44%	\$3,888,889	124.2%	14.04%
Equity (3.40%)	<u>(757,768)</u>	<u>(24.2%)</u>	<u>14.04%</u>

Composite Cost of Total Capital 14.04%

RATE BASE

13. The Applicant proposed an average original cost-depreciated rate base of \$180,697.

14. During the course of cross-examination, the Montana Consumer Counsel questioned the accuracy of the Applicant's proposed average original cost-depreciated rate base as it related to the Applicant's treatment of "Contributions in Aid of Construction" (CIAC) and "Credit for Accrued Property Taxes." The Consumer Counsel contended that the Applicant's treatment of these items resulted in an overstatement of rate base on which the Applicant

should be allowed a return.

15. Both the Montana Consumer Counsel and the Applicant submitted briefs concerning the issue of appropriate treatment of CIAC in determining rate base.

The Montana Consumer Counsel's brief provided numerous case cites supporting its position that it was inappropriate to allow the Applicant to add back accumulated depreciation on CIAC in the amount of \$13,588 when determining rate base on which the Applicant should be allowed a return. The Applicant, who utilized the add back of accumulated depreciation on CIAC procedure, conceded in its reply brief that the position presented by the Consumer Counsel represented the majority case law view for treatment of CIAC in determining rate base.

The Commission, having considered the arguments presented by the Applicant and the Consumer Counsel, finds that the Applicant should not be allowed to add back the accumulated depreciation on CIAC in the amount of \$13,588 for purposes of determining rate base, because it results in the ratepayer paying a return on funds that have been provided by the ratepayer.

16. The Consumer Counsel also took the position that the Applicant should not be allowed to expense depreciation on CIAC.

The Commission is cognizant of the fact that the plant provided by CIAC is plant that has been provided by the ratepayer, and, therefore, should not be included in rate base and allowed to earn a return to the investor. The question of allowing depreciation expense on CIAC is a philosophical one and requires examination.

In general terms depreciation is for the purpose of recovering original investment in property over the useful life of that property, and is generally recognized as a lost usefulness of the asset or asset group. An allowance for depreciation on CIAC is based on the assumption that the plant provided by CIAC will have to be replaced at the end of its useful life, and, by allowing depreciation expense on CIAC, the utility will have funds available to replace this plant without need of further CIAC.

The allowance for depreciation on CIAC is, therefore, not considered depreciation, but rather is an allowance for replacement of the plant provided through CIAC. This method of accumulating funds for replacement of the plant provided through CIAC prevents the utility from increasing its rate base, except to the extent the replacement cost of the contributed plant exceeds the amount of the original CIAC.

This method of funding for replacement of the plant provided through CIAC was not fully explored on the record in this docket; therefore, the Commission-reserves ruling on the propriety of this funding mechanism. The Commission finds the Applicant should be allowed to continue its practice of expensing depreciation on CIAC, until such time as the Commission has adequate information on the record to make a final ruling. The rationale behind allowing continuance of the depreciation in this docket centers around a lack of information, relative to who provided the original CIAC and whether the philosophy of allowing a depreciation expense is an overall benefit or detriment to the ratepayer.

17. In prior proceedings before this Commission, the Applicant has used simple accumulation of monthly tax accruals for purposes of determining working capital available from property tax accruals. In this docket, the Applicant revised its procedure and proposed that working capital available from property tax accruals be determined based on monthly use of funds coming from the cumulative monthly tax accruals as limited by cumulative monthly funds available. In other words, the Applicant is proposing that the Commission accept the analysis made on page 2 of 38.5.141, Applicant's Exhibit No. 2, as a lead-lag study.

The Commission rejects the Applicant's proposed modification because the analysis limits the examination of the timing of receipts and payments to only two accounts, which is insufficient to produce any meaningful data.

The Commission finds, for purposes of determining cash working capital available from property tax accruals, it is appropriate to continue the procedure that has been used and accepted in prior proceedings before this Commission.

18. Consistent with the Applicant's proposed modification outlined above, the Applicant proposed that the "Credit for Accrued Property Taxes" should be in the amount of \$1,990. Using the procedure consistently accepted by the Commission in the past, the "Credit for Accrued Property Taxes" increases to \$10,813. Therefore, the Commission finds that the Applicant's proposed original cost-depreciated rate base should be decreased by \$8,823.



19. Based upon the preceding Findings of Fact, the Commission finds the Applicant's original cost-depreciated rate base should be \$158,286.

#### OPERATING EXPENSES

20. The Applicant, in its Exhibit No. 4, proposed total test period operating revenue deductions of \$280,361.

21. The Commission has determined the following adjustments to test period operating revenue deductions are appropriate:

a. Fringe benefit expense for salaried employees should be reduced by \$1,612 to reflect savings in this account as a result of employee retirements. This expense savings was calculated by using the ratio determined by the Applicant on page 157.3a of Exhibit No. 4 and applying it to expense savings resulting from the employee retirements ( $\$5,339 \times .302 = \$1,612$ ).

b. Pension expense should be increased by \$1,453 to reflect the actual pension costs being charged BWC as calculated by its parent company, Anaconda Minerals.

22. The Montana Consumer Counsel, during its cross-examination of Company witnesses, proposed that salary expense associated with employee retirements should be amortized over a period of years, instead of being charged as a current cost during the test period as proposed by the Applicant. The Consumer Counsel properly states in its initial brief that this item of expense is nonrecurring in nature, and that traditional rate-making

treatment of this expense would dictate that it be amortized.

The Commission on many occasions has required utilities under its jurisdiction to amortize items of expense which are nonrecurring in nature. In this instance, given the financial condition of BWC, its mounting operating losses, its attempts to economize through re-negotiation of its collective bargaining agreements and implementation of an early retirement program to decrease future operating expenses, the Commission finds it appropriate to charge salary expense associated with employee retirements as a current cost in an effort to maintain the financial integrity of BWC. To reflect the expense savings that will accrue to BWC in future periods, the Commission should require BWC to file revised tariffs that will become effective January 1, 1985, which reflect a reduction in its overall revenue requirement amounting to \$42,505, which equals the expense savings, including fringes, associated with salaried employee retirements ( $\$32,646 \times 1.302 = \$42,505$ ).

23. Based upon the preceding Findings of Fact, the Commission finds the Applicant's total operating revenue deductions, prior to January 1, 1985, to be \$280,202, and subsequent to January 1, 1985, to be \$237,697.

#### OPERATING REVENUE

24. The test period operating revenues are not a contested issue in this case. The Applicant utilized the 12 months ended December 31, 1982, to determine the test year revenues under the rates

which became effective November 15, 1982. Total test year revenues of \$286,597, as calculated by the Applicant, are accepted by the Commission.

Operating Income for BWC is found to be \$6,395:

Operating Revenue	\$286,597
Operating Deductions	<u>280,202</u>
Operating Income	\$ 6,395

#### REVENUE REQUIREMENT

Rate Base	\$158,286
Rate of Return	<u>14.04%</u>
Return Requirement	\$ 22,223
Adjusted Balance Available for Return	6,395
Return Deficiency	15,828
Revenue Deficiency	15,842
MCC Tax at .09%	<u>14</u>
Income Available for Return	\$ 15,828

25. In order to produce a return of 14.04 percent on the Applicant's average original cost-depreciated rate base, the Applicant will require additional annual revenues in the amount of \$15,842 from its Anaconda, Montana, water utility.

#### RATE DESIGN

26. The rate design proposed by the Applicant was not challenged by any party participating in this proceeding. The rate design appears to equitably spread the increase among the various customer categories, therefore, the Commission accepts the Applicant's proposed rate design.

## MISCELLANEOUS

27. In Order No. 4897a, the Commission discussed the Applicant's practice of providing free water service to certain consumers connected to its facilities and ordered that the Applicant discontinue this practice. Order No. 4897a provided that the Applicant would start assessing those consumers that had been receiving free water service one-third of the appropriate charge and that subsequent rate orders would be used to phase in the remaining two-thirds of the full charge.

The Commission finds that the Applicant should start assessing consumers that had been receiving free water service two-thirds of the respective consumer's appropriate charge.

## REBATES

28. Because the interim increase in this docket of \$19,718 is greater than the final increase of \$15,842, a rebate condition has developed. In addition, Ordering Paragraph No. 4 of Interim Order No. 4978 established a rebate interest rate of 14.04 percent.

29. The Commission finds that BWC must compute over-collections, by customer class, that result from the differential between the interim rates that went into effect on May 2, 1983, and the rates that would have been in effect assuming a uniform percentage increase for a \$15,842 final increased revenue requirement.

30. Interest must be accrued from the time BWC received revenues,

based on interim rates, until the time the final rates become effective. From communication between the Commission staff and the Company, the Commission understands that the customer class over-collections, for rebate purposes, cannot be computed to take effect until the April or May billing; the May billing is the latest acceptable date to the Commission for the-Company to make rebates to customers.

31. The Commission understands (based on Commission staff/Company communication) that the most efficient means of rebating the over-collection to each customer class is on a one-time credit basis.

32. The Commission understands (from Commission staff/Company communication) that the most efficient means of rebating each customer class's total over-collection is through calculation of the percentage differential between the interim and permanent revenue level and then applying this percentage differential to the actual customer billings during the period the interim rates were in effect. The Commission finds this proposal to be reasonable and, therefore, accepts the procedure.

33. When the rebate is made, each customer's bill should include an explanation that the rebate amount is due to a combination of a lower final revenue requirement, relative to the interim, and interest at 14.04 percent.

#### CONCLUSIONS OF LAW

1. The Montana Public Service Commission properly exercises jurisdiction over the parties and subject matter in this

proceeding. Section 69-3-102, MCA.

2. The Commission afforded all parties interested in this proceeding proper notice and an opportunity to participate. Section 69-3-303, MCA.

3. The rates approved herein are reasonable, just, and proper. Section 69-3-201, MCA.

#### ORDER

NOW THEREFORE, IT IS ORDERED THAT:

1. Butte Water Company shall file rate schedules which reflect an increase in annual revenues of \$15,842 for its Anaconda, Montana, water service. The increased revenues shall be generated by increasing rates and charges to all customer classifications and assessment of two-thirds of the appropriate charge for consumers previously receiving free water service.

2. The revenues approved herein are in lieu of those approved. in Order No. 4978.

3. The rates approved herein shall not become effective until approved by this Commission.

4. Butte Water Company must, for each customer class, submit for verification detailed working papers showing the actual over-collection, with interest at 14.04 percent, that will be rebated.

5. Butte Water Company shall file revised rate schedules on or

before January 1, 1985, reflecting a reduced revenue requirement as provided in Finding of Fact No 22.

6. A full, true, and correct copy of this Order shall be sent by first class mail to the Applicant and to all parties of record.

7. DONE IN OPEN SESSION this 5th day of March, 1984, by a vote of 3 - 0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

---

THOMAS J. SCHNEIDER, Commissioner

---

JOHN B. DRISCOLL, Commissioner

---

HOWARD L. ELLIS, Commissioner

ATTEST:

Madeline L. Cottrill  
Commission Secretary

(SEAL)

NOTE:

Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See ARM 38.2.4806.